[2016] UKFTT 255 (TC)

# TC05030

**Appeal number: TC/2015/02520**

***VAT – VAT Assessment in default of returns by taxpayer partnership which had traded above VAT registration threshold – retrospective registration – VATA 1994 Schedule 1 paragraphs 1 and 3 – penalty for late registration – s 70 VATA 1994 – whether reliance on advice of accountant a reasonable excuse – no – whether assessment exceeded best judgement calculation – yes – appeal allowed in part***

**FIRST-TIER TRIBUNAL**
**TAX CHAMBER**

**JOSHUA READY and LEANDA JONES t/a THE OPEN KITCHEN CAFE** — **Appellants**

**- and -**

**THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS** — **Respondents**

**TRIBUNAL: JUDGE MICHAEL CONNELL**
**MEMBER TERRY BAYLISS**

**Sitting in public at Tribunal Appeals Service, Centre City Tower, Hill Street, Birmingham on 18 November 2015**

**The Appellants in person**

**Mr David Ridley, Officer of HMRC, for the Respondents**

DECISION

## The Appeal

1. This is an appeal by Mr Joshua Ready and Ms Leanda Jones trading as The Open Kitchen Cafe ("the Appellants") against an assessment for under declared VAT of £29,609.45 following a decision by HMRC ("HMRC") that the Appellants' partnership should have been registered for VAT for the period 1 April 2009 to 31 March 2013 during which it had traded above the VAT registration threshold. The Appellants also appeal a Belated Notification Penalty in the sum of £3,331 for the late registration.

2. The Appellants do not dispute that they failed to notify their liability to be registered for VAT at the proper time, that being 1 April 2009, or that the relevant default period is from that date to 31 March 2013 when the business ceased to trade and the partnership ended.

3. The Appellants' grounds of appeal are that they did not know that they were liable to be registered for VAT because, so far as they were aware, their turnover did not exceed the relevant VAT threshold for the years 2009 to 2013. They say that their former accountant had prepared the business accounts for the period under appeal and had incorrectly advised them that their turnover did not include zero rated foods. When zero rated sales were included, their turnover had exceeded the VAT registration threshold. Had they been aware of the necessity to register, they would have done so.

## Factual Background

4. The Appellants traded in partnership as the Open Kitchen Cafe, from 20 Bridge Street, Stourport, DY13 8UT.

5. On 15 September 2014 HMRC wrote to the Appellants advising them that from completed self-assessment returns it appeared that their business should have registered for VAT. HMRC asked the Appellants to complete and return a VAT questionnaire.

6. The Appellants returned the questionnaire duly completed with relevant documentation relating to the business's weekly/yearly takings figures.

7. On 23 October 2014 HMRC wrote to the Appellants stating that, based on the information provided, the business was liable for VAT registration from 1 April 2009 to 31 March 2013 when the partnership ceased to trade (Mr Ready becoming a sole trader). The letter requested input and output tax figures for this period.

8. On 26 November 2014, the Appellants wrote to HMRC saying that when they bought the cafe it was not VAT registered, but that they now realised the business had traded over the threshold and should have been registered for VAT. They said that

they were told by their accountant that the zero rated items were not included in the threshold. They argued that they had acted in good faith and relied upon their accountant's advice. Had they known that zero rated items should have been included for the purposes of calculating their turnover, they would have operated the business differently. They would have closed their business for two days a week. They felt that the assessment was unfair.

9. The Appellants included details of their input and output tax for the period April 2009 to 2013. They calculated their total liability figures as:

| Year | Output tax | Input tax | To Pay |
|---|---|---|---|
| 2010 | 11,196.17 | 5,109.45 | 6,086.72 |
| 2011 | 12,114.43 | 5,550.20 | 6,564.23 |
| 2012 | 14,532.00 | 6,005.85 | 8,526.15 |
| 2013 | 15,323.90 | 6,891.55 | 8,432.35 |
| | | | 29,609.45 |

10. On 11 December 2014, HMRC issued a decision letter to the Appellants advising them that they were required to be registered for the period 1 April 2009 to 31 March 2013. The amount of tax payable was £23,987.88. A Belated Notification Penalty of £3,598 was also payable.

11. The Appellants responded saying that they understood that they would have to pay the assessed VAT, but that the imposition of a penalty was unfair. Further they "did not have the money to pay the tax let alone the penalty".

12. After a further exchange of correspondence, on 5 January 2015 the Appellants requested a Statutory review of the decision.

13. On 19 February 2015 a review conclusion letter was issued by HMRC upholding the original decision to register the business, but increasing the assessment to £29,609 (as per the Appellants' calculations). The penalty was reduced to £3,331 to take into account the Appellants full extent of co-operation and disclosure.

14. The Appellants lodged an appeal with the Tribunal Service on 12 March 2015.

**Evidence**

*Officer Pickerill's evidence*

15. The combined bundle of documents included copy extracts from the partnership tax returns for the years 2009-13; the Appellants' completed form HEG - 02 (a generic questionnaire which provided details of the Appellants' business including monthly income by reference to takings for items 'sit in' and 'take out', for the years

2009-13); a chronological summary of the Appellants' takings by reference to the prevailing VAT registration threshold; the witness statement of Officer Andrew Pickerill, the HMRC officer who undertook a check of the Appellants' VAT status (Officer Pickerill also gave oral evidence to the tribunal); copy relevant correspondence; copy relevant legislation and case law authority.

16. In his witness statement Officer Pickerill said that Mr Reddy had provided all requested information including details of the business turnover. Officer Pickerill said that he allowed all 'take out sales' to be zero rated and only 'eat in sales' to be standard rated. He used the business total sales turnover figures provided by Mr Ready and entered them into an excel spreadsheet which calculated whether the business turnover had exceeded the VAT threshold. From the information provided by Mr Ready it was established that the partnership should have been registered for VAT from 1 April 2009 to when the partnership ceased on 31 March 2013.

17. To enable him to continue with his enquiries Officer Pickerill requested the business's output tax and input tax figures for the period 1 April 2009 to 31 March 2013, which were duly provided by the Appellants, from which he calculated the tax due figure to HMRC as £23,987.88 and a Belated Notification Penalty because the business had failed to register for VAT at the appropriate time.

18. Officer Pickerill said that following the statutory review on 19 February 2015 it became apparent that he had made an error when calculating the tax due figure. He had interpreted the yearly output tax/ input tax figures provided by the Appellants as calendar years not financial years. This meant that he had understated the total tax due figure and that the tax due figure to HMRC increased from £23,987 to £29,609 (which accorded with the Appellants' own calculations). With regard to the Belated Notification Penalty it was decided that a 25% mitigation should be allowed to take into account the level of co-operation throughout the enquiry. Taking into account the increased tax due figure and the 25% mitigation to be allowed the new penalty amount was calculated as £3,331.

19. In evidence to the Tribunal, Officer Pickerill said that he had relied on the weekly turnover figures provided by the Appellants in calculating the rolling total.

20. Officer Pickerill said that the Appellants had not provided any primary evidence of takings relating to standard rated supplies and zero rated supplies and so he relied on the figures provided by the Appellants. If he had to assess the amount of VAT due on standard rated items to best judgement he would have allowed 30% as the proportion to be deducted from the total turnover, in order to exclude zero rated take away items.

21. At the hearing, neither Mr Ready nor Ms Jones gave evidence. Indeed they were not disputing HMRC's calculations which they accepted were based on the turnover figures they themselves had provided.

## Relevant legislation

22. The law relevant to the appeal is contained in:

VATA 1994 ("VATA")

'Taxable supplies'

Section 4(2) A taxable supply is a supply of goods or services made in the United Kingdom other than an exempt supply.

Sch 1, Para 1(1) sets out when an unregistered person making taxable supplies becomes liable to be registered:

> "1(1) Subject to sub paragraph (3) to (7) below, a person who makes a taxable supplies but is not registered under this Act becomes liable to be registered under this schedule
>
> a) at the end of any month, if the value if his taxable supplies in the period of one year then ending has exceeded (relevant VAT threshold); or
>
> b) at any time, if there are reasonable grounds for believing that the value of his taxable supplies in the period of thirty days then beginning will exceed (relevant VAT threshold)."

Sch 1, Para 1(3) - sets out the rules regarding exception from registration:

> "A person does not become liable to be registered by virtue of sub-paragraph (1) (a) or (2)(a) above if the Commissioners are satisfied that the value of his taxable supplies in the period of one year beginning at the time at which, apart from this subparagraph, he would become liable to be registered will not exceed £(threshold)"

Sch 1, Para 5, - sets out the rules regarding notification of liability and registration.

Sch 1, Para 6(2), - permits the Commissioners to register with effect from the period when liability arises.

Section 67 –

> "67(1) In any case where-
>
> (a) a person fails to comply with any of the paragraphs 5, 6, 7 and 14(2) and (3) of Schedule 1 .....
>
> he shall be liable, subject to subsections (8) and (9) below, to a penalty equal to the specified percentage of the relevant VAT or, if it is greater or the circumstances are such that there is no relevant VAT, to a penalty of £50."

Penalty rates are covered by, Section 67(4) which allows the Commissioners to consider charging a penalty for the belated notification of liability and sets out how the amount charged is to be calculated. The taxpayer is liable to a penalty equal to the specified percentage of the 'relevant VAT'. The 'relevant VAT' is defined under s 67(3) as the VAT due for the period from when the taxpayer should have been

registered to when he did in fact notify HMRC of his liability to register. Under s 67(4)(c) the specified percentage penalty is 15% of the relevant VAT payable in any case where the time between the date on which the taxpayer ought to have registered for VAT and notified HMRC of his liability to register is greater than 18 months.

Section 68(8) provides that a failure to register under s 67(1) shall not give rise to a penalty if the Tribunal is satisfied that there is a reasonable excuse for the failure to register.

Section 70(1)(b) provides that, where reliance is placed on any other person to perform any task, neither the fact of that reliance nor any dilatoriness or inaccuracy on the part of the person relied upon is a reasonable excuse.

Section 70(4)(c) VATA provides that the fact that the tax-payer or person acting on his behalf has acted in good faith cannot be taken into account by the Tribunal in any exercise of its powers to mitigate or cancel the penalty.

Section 71 - provides that an insufficiency of funds to pay any tax due or the reliance on any other person cannot be considered a reasonable excuse.

Section 73 - allows assessments to be made where Returns have been made but are incomplete or incorrect, or have failed to be made, in an amount of VAT to the best judgement of the Commissioners.

Section 83 - sets out matters that carry a right of appeal.

**The Appellants' case**

23. The grounds of appeal as set out in their Notice of Appeal are:

> "We are a small cafe in a small seasonal tourist town and trade 7 days a week. Most importantly we were misinformed by our accountant that non-vatable sales are not included in the vat threshold. We have traded like this for 7 years and were only taking advice from our accountant. We have considered taking legal advice. The liability is for £49,727.03 [including a further assessment for 2014 against Mr Ready trading as a sole proprietor] whereas in the period 2009 to 2014 our net profit has been £82,287.65 (last 6 years) which means our profit has really been £32,560.62. We hope this shows that we have a small profit margin on our sales and have not charged vat on what we sell ( bacon sandwich £1.50) and open 7 days. We have small children and employ staff to cover our days off. We cannot pay the amount assessed. We would have operated the business in a totally different way and closed 2 days a week or charged vat on our sales. We feel it is really unfair to pay back that amount of money when we cannot go back and ask all our customers to pay vat on their purchases. We have no assets and live above the cafe and this has really scared us and we do not know what to do. The cafe did not make enough money in the last 6 years to pay this amount of debt and we could become bankrupt. We agree that there should be money paid as that's the law but we do not know how. The business is now vat registered and prices have been up and business is still ok. The penalty is also unfair as we did not do this on purpose and not tried to evade vat.
>
> If we knew that we were advised wrong we would have charged vat on our sales and would have been able to pay. I run the business very well and this has been our life for

the past 7 years I am now 30 years and depressed that this has happened as it's not our fault."

24. At the hearing Mr Ready reiterated the Appellants' grounds of appeal as set out in the Notice of Appeal.

**HMRC's case**

25. A trader becomes liable to be registered once his turnover breaches the registration threshold, unless it is considered that an exception from liability to be registered can be granted.

26. With regard to exception from registration, normally, a person would not become liable to register for VAT if they could show that the value of their taxable supplies for one year, after the time they became liable to register did not exceed the stated Deregistration limit [Sch1, para 1(3)]. As a concession to Liable No Longer Liable (LNLL) traders, the period to which their liability to account for VAT ends is determined not by the deregistration limit in force at the time, but the registration threshold.

27. The rolling turnover figures for the Appellants' business show that their turnover exceeded the registration and deregistration limits throughout the period of the LNLL period.

28. When considering an exception retrospectively, it is only information that would have been available at the time the liability to register first arose that can be considered.

29. The Appellants say that they were misinformed by their accountant that only standard rated sales should be taken into consideration when calculating their VAT turnover. They say that approximately 20% of their sales were zero rated. The annual declared income of the business in the period 2009-10 to 2011-12, applying an 80% standard rated apportionment and the VAT threshold for each year shows the following figures:

| Year | SA Turnover | 80% | Threshold |
|---|---|---|---|
| 2008-09 | 78,775 | 63,020 | 67,000 |
| 2009-10 | 85,072 | 68,058 | 68,000 |
| 2010-11 | 86,715 | 69,372 | 70,000 |
| 2011-12 | 97,806 | 78,245 | 73,000 |

30. HMRC do not accept that the Appellants have good reason for not registering for VAT in these years. Even if the Appellants were only comparing their standard rated sales to the VAT threshold they should have contacted HMRC during both the 2009-10 and 2010-11 tax years when they breached the annual turnover levels. The failure of the Appellants to register for VAT in these two years is an indicator that even the

incorrect advice of the accountants was being ignored. The Appellants appear to have totally disregarded any liability to register for VAT through the four tax years.

31. The Appellants have provided no evidence that would have been available at the date of the breach that would satisfy HMRC that for each year their turnover in the following twelve months would not breach the relevant VAT threshold.

32. With regard to the Established Date of Registration (EDR), under VATA 1994 Schedule 1 para 1(1)(a) a person becomes liable to be registered if the value of his taxable supplies in the period of one year then ending, exceeds the registration threshold. Schedule 1 para 5 states that once the registration threshold has been exceeded, the trader has 30 days in which to notify their liability to register. For the time periods concerned with this case, the registration limits were: Period 1 April 2008 to 30 April 2009 - £ 67,000.

33. The Appellants exceeded this limit at the end of February 2009 - £68,052. They then had 30 days in which to notify their liability to register i.e. by 30 March 2009 [Sch 1, para 5(1)]. This gave a registration date of 1 April 2009 [para 5(2)]. The partnership remained above the registration limit until it ceased trading at the end of March 2013. Therefore the registration period is 1 April 2009 to 31 March 2013.

34. Reliance upon their accountant did not amount to reasonable excuse under s 71(1)(b) as set out above, which provides that neither reliance upon another person, nor that other person's inadequacies in discharging their responsibilities, may amount to reasonable excuse.

35. The Appellants accept that the business made taxable supplies and was thus liable to be VAT registered. HMRC have not been provided with any grounds which show a reasonable excuse for the late registration.

36. The Appellants' arguments that they are unable to pay the amount of tax now due has no legal basis in HMRC's view – s 71 VATA.

37. With regard to the Belated Notification Penalty, the penalty rates are covered by the VAT Act 1994, s 67, sub-section (4). In this case HMRC submit that appropriate category is "exceeding 18 months - 15% of the relevant VAT due". HMRC were aware of the partnership's requirement to be registered on receipt of the documents supplied on 16 October 2014, which is more than 18 months after the EDR date of 1 April 2009, and therefore a 15% penalty is appropriate.

38. Once a penalty has been calculated, if the Commissioners are satisfied that there was a reasonable excuse for the error, then the liability to the penalty will be waived. In the reasons given for the error, the partners have advised that they were reliant on their accountant for advice and that they believed that the zero rated sales should not be included in the taxable turnover. This cannot be considered a reasonable excuse for not registering at the correct time – s 70(1)(b) VATA.

39. Mitigation - (Section 70). Where reasonable excuse does not exist, if the Commissioners are satisfied that there are mitigating circumstances, they can reduce

the penalty by any amount they see proper, and where appropriate to nil. Guidance at VCP11747 advises that mitigation can be given when there has been co-operation in quantification of the arrears.

40. In this case the partners promptly completed and provided the weekly takings figures on which the EDR and assessment are based. Therefore there is scope for mitigation for the assistance given in quantifying the error. VCP11747 states that in these circumstances mitigation of up to 25% should be given.

**Decision**

41. The Tribunal finds that HMRC's decision, that the Appellants' business should be registered from 1 April 2009 to 31 March 2013, is correct. The Appellants have not shown a reasonable excuse for their late registration. We concur with HMRC's submissions as set out in paragraphs 25 – 36 above. Ignorance of the law and reliance upon another for advice is not a reasonable excuse. For the above reasons we find that the Appellants do not have a reasonable excuse for late registration for VAT

42. In arriving at the assessment, Officer Pickerill relied on the Appellants' figures with regard to the percentage of standard and zero rated sales and also the Appellants' calculation of VAT due. On reviewing the figures however it is clear that the total annual turnover figure provided by the Appellants and on which Officer Pickerill had calculated VAT due, included zero rated sales. For example, the total turnover for 2009 -10 according to the Appellants' and Officer Pickerill's spreadsheet calculations, was £85,066, in respect of which the VAT element according to the Appellants would have been £11,196.17, assuming a VAT rate of 15%. It was on the figure of £11,196.17 that VAT due was calculated at £6,086.72 for 2009-10. No allowance was made for zero rated sales and furthermore the change in the VAT rate from 15% to 17.5% during the period 2009-10 had not been taken into account.

43. On checking the Appellants' figures it was also clear that there were a few minor mathematical errors in the sales records. There was also no primary evidence to support the Appellants' estimate of zero rated sales at a consistent level of 20% of total sales throughout the period of assessment. Officer Pickerill's best judgement estimate would have put the level at 30% and standard rated sales at 70% and that is the level at which the assessed VAT on the facts and circumstances should have been assessed.

44. We therefore find that the HMRC's calculations over assessed the VAT due. We set out below the Tribunal's calculation of the correct amount of VAT due.

| Year | Sales | Std Rate (70)% | VAT Rate | Output Tax | Year Total | Input Tax | Net Payable |
|---|---|---|---|---|---|---|---|
| 2009/10 | | | | | | | |
| 01/04/2009 - 31/12/2009 | 69060.73 | 48342.51 | 15.00% | 6305.54 | | | |
| 01/01/2010 - 31/03/2010 | 16005.54 | 11203.88 | 17.50% | 1668.66 | 7974.20 | 5109.45 | 2864.75 |
| 2010/11 | | | | | | | |
| 01/04/2010 - 31/12/2010 | 69191.70 | 48434.19 | 17.50% | 7213.60 | | | |
| 01/01/2011 - 31/03/2011 | 17885.14 | 12519.60 | 20.00% | 2086.60 | 9300.20 | 5550.20 | 3750.00 |
| 2011/12 | | | | | | | |
| 01/04/2011 - 31/03/2012 | 100469.06 | 70328.34 | 20.00% | 11721.39 | 11721.39 | 6005.85 | 5715.54 |
| 2012/13 | | | | | | | |
| 01/04/2012-31/03/2013 | 90226.38 | 63158.47 | 20.00% | 10526.41 | 10526.41 | 6891.55 | 3634.86 |
| | | | | | | | **15965.15** |

Belated Notification Penalty 15965 x 15% x 75% = £1796

45. The assessment is therefore reduced to £15,965.15

46. HMRC mitigated the penalty by 25% because of the Appellants' co-operation and assistance in quantifying the VAT due. We regard the amount of mitigation applied by HMRC as correct, but the penalty, as shown in the table above, is reduced to £1,796 because of the reduction in the assessment.

47. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

**MICHAEL CONNELL**
**TRIBUNAL JUDGE**

**RELEASE DATE: 18 April 2016**